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Policy Forum Article

The European Union and China: The Need for a More Politicised Relationship

Kerry Brown* and Sam Beatson

Abstract

China and the European Union (EU) in 2016 have one of the largest economic relationships to the world, with a network of strategic dialogues covering areas from environment to agriculture. Despite this, their relationship is a hard one to encapsulate. President Xi Jinping's idea of a 'civilisational' partnership seem abstract, but at least opens up the possibility of the EU conceptualizing its relationship with China as not solely transactional, but something more political. This paper argues that conferring Market Economy Status on China will be a key issue in marking this transition between the EU seeing its link with China solely in economic terms, and looking for a stronger political dimension. The conclusion is that both sides can no longer pretend they are simply trade blocks interacting with each other.

1. The European Union and China: Origins

The relationship between the European Union (EU) and China is one of the most important in the world today. And in terms of trade and quantifiable flows of goods, it is an impressive one. In 2014, bilateral trade amounted to €466 billion (Figure 1). China was the EU's largest source of imports and second largest export market. Of the total trade of what is, in effect, the world's greatest trade bloc, China constituted 13 per cent of all of the EU's business.¹ This consisted overwhelmingly of trade in industrial products, accounting for 98 per cent of the EU's imports and 95 per cent of exports to and from China. Over the same period, only the United States, with a combined total of US \$698 billion (€625 billion) had greater levels of trade with the People's Republic (PRC).² In terms of inward and outward investment, too, the links are strong and strengthening. By the end of 2013, the EU had €119 billion invested in China, 50 per cent more than that number 3 years earlier. But this was still only 2 per cent of foreign direct investment (FDI) stocks in the PRC.³ China had a mere €16 billion invested back in the EU, coming in at less than 1 per cent of its overall FDI stocks

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1. Source: European Commission Directorate General for Trade: http://trade.ec.europa.eu/doclib/docs/2006/september/tradoc_113366.pdf, accessed 13th March 2016.

2. Source: United States Census Bureau, <https://www.census.gov/foreign-trade/balance/c5700.html>

3. Source: Eurostat: http://ec.europa.eu/eurostat/statistics-explained/index.php/File:EU_FDI_stocks_in_BRIC_countries,_2008-2012,_EUR_billion.png

(Figure 2).⁴ The much smaller economy of the Hong Kong Special Administrative Region aggregate total of FDI into the 28 EU member states comes to triple that directly sourced from the PRC. However, given the growth inflows over the last several years, this source may have reached its zenith.

There is nothing particularly strange about the importance of the EU Chinese economic relationship. The original diplomatic recognition conferred on each other predated the existence of the EU and was between the European Economic Community (EEC) and the People's Republic in 1975. This was formalised by way of the document, which still stands as the legal basis of the relationship to this day, the 'EEC Trade and Economic Cooperation Agreement'. In its preamble, this agreement 'aims to introduce a new stage, to promote and intensify trade and to encourage the steady expansion of economic cooperation in the mutual interest of both parties'.⁵ It reads as a solidly trade focused agreement, granting most favoured nation status on China for a number of goods classes.

One of the anomalies is that despite no agreement replacing the 1985 accord, with the implementation of the Maastricht Treaty in 1994 bringing the EU into existence, its function and status changed. Far from being a purely common trading block, the new treaty set out a number of social and political aspirations, some of which proved contentious even within the new EU. The Social Chapter, for instance, encoded certain working rights and social welfare levels, which the United Kingdom for one negotiated an opt-out clause for. The EU also started to figure much more strongly as a community of values, not just economic expediency, and became keen on promoting this beyond its borders. From 1995 to 2015, it also saw the accession of a group of new states, more than doubling its membership by 15. For China, therefore, a relationship which had initially focused purely on trade and transactions

developed a new and less straightforward dimension after 1994, one in which the EU asserted a number of values and ideas which became part of its internal and external identity. This legacy from their origins as simply having a trading relationship and interaction based on that has never gone away, despite the clear fact that the EU now is not the straightforward actor that the EEC was. The two in the twenty-first century are still partially pretending to be living in another era. No wonder they had challenges after 2000 when it was clear this earlier model was no longer fit for purpose, and they needed to think about themselves and then their relationship with each other in a very different way.

2. The Search for a New Framework

The period from 2002 to 2014 can be categorised as one of mutual learning and was dominated by an almost unconscious deepening politicisation of the relationship despite neither side being willing to fully admit this. Because of this cognitive mismatch, it was marked by each side losing some of their illusions about the other. This is neatly evidenced by two Chinese State Council White Papers, (formal articulations of government policy) one issued in 2003 and the second in 2014. A comparison of the language used in each marks this journey of disillusionment in China's eyes. The 2003 paper acknowledges that 'the European Union (EU) is a major force in the world. The Chinese Government appreciates the importance the EU and its members attach to developing relations with China'. Under the political chapter, the paper simply asks the EU to 'abide' by the One China policy regarding Taiwan, to 'promote the EU's understanding of Tibet' and to 'continue the human rights dialogue'.⁶

Twelve years later, the language was different. In the intervening years, a number of events had posed hard questions about what each meant to the other beyond raw trade and goods, and shown a paucity of response on

4. http://ec.europa.eu/eurostat/statistics-explained/index.php/File:BRIC_FDI_stocks_in_the_EU_2008-2012,_EUR_billion.png

5. EUR Lex, European Law Database, <http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=uriserv:r14206>

6. China EU Policy Paper, Office of the State Council, 2003, at <http://china.org.cn/e-white/20050817/index.htm>

Figure 1 Trade in goods by sector 2006–2015

EU-China Imports, Exports & Trade Balance in Goods & Services

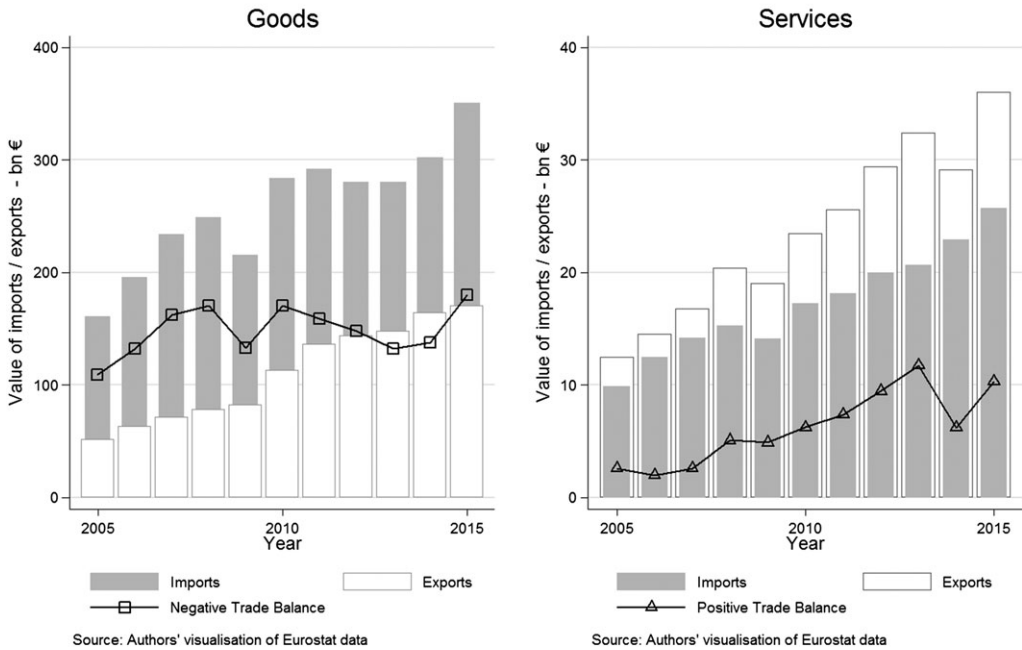
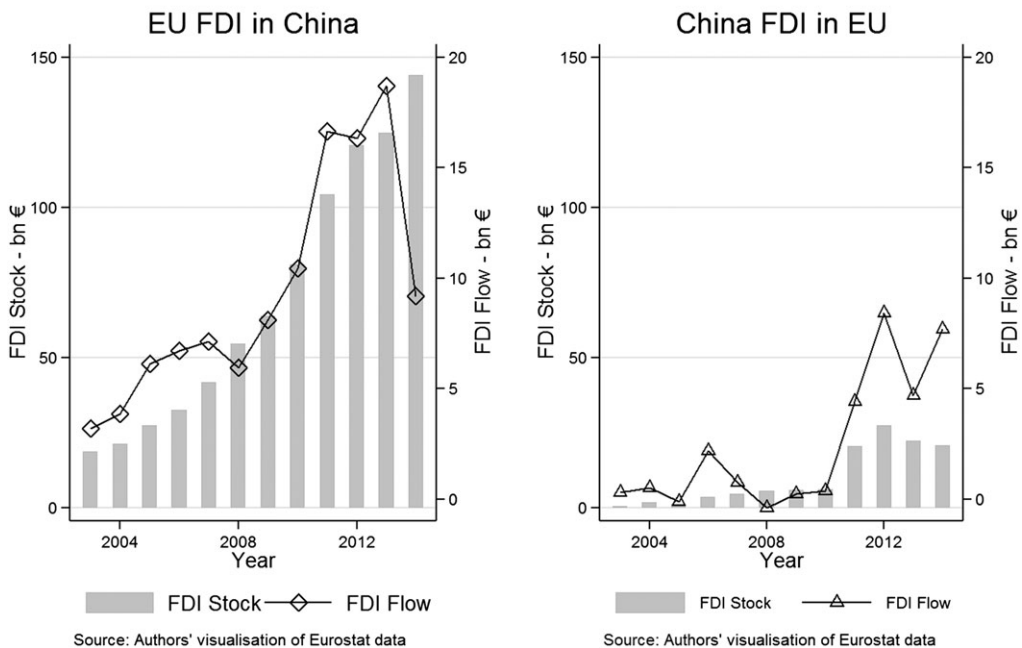


Figure 2 Foreign direct investment (FDI) flow and stocks European Union–China and China–European Union 2006–2015. NB. 2014 flow data subject to revisions.

FDI stock & flows of and between the EU and China



both sides. The first of these was the failure after what were (at least in Chinese eyes) initially promising moves of the EU to lift the arms embargo imposed on the PRC after the Tiananmen Square Massacre in 1989. This had been as a result of US pressure, and had shown that in the security and military sphere, the EU answered almost wholly to Washington. The second was the continuing refusal of the EU to grant China market economy (ME) status, even though the PRC had entered the World Trade Organisation by December 2001 and felt it had implemented largely market friendly policies. The third was a series of meetings at head of government or head of state level between major European countries and the Dalai Lama, the exiled Tibetan religious leader.

China has long been sensitive to what is perceived as international interference in matters it regards as internal affairs. The ruling Communist Party of China (CPC) is therefore quick to react with strong diplomatic language and actions to behaviour by other states and actors construed as supporting political, social and religious separatism within its borders. Defence of the unified and singular Chinese nation state (currently embracing the PRC, and including Hong Kong and Macau Hong Kong Special Administrative Regions to the south, Taiwan [island] by the PRC to the east, and the Tibet and Xinjiang Uyghur autonomous regions to the south and northwest) are priorities for Beijing. Any moves by a party like the EU or its member states to become involved, or to be perceived as becoming involved with these issues, is met with great resistance. These are clearly signalled in the 2003 EU White Paper. The EU's failure to come up earlier with a coherent unified response to these issues meant it was often shown to be disunited, and often manipulated by the Chinese. A harder sense of its political identity would have helped prevent this.

There was another factor that had a profound impact on the EU China relationship, and showed well how even matters firmly in the economic realm carried immense political meaning, indicating how the two are increasingly interconnected. From 2008, the EU, once a haven of economic stability and

predictability, became beset by crises in the Eurozone. This eroded its reputation in terms of competent financial governance, but it also raised questions over its political stability. With the expansion of the Union to 28 states by 2015, too, the coherence internally of the EU became questionable to Chinese leaders. Their language over this period became more qualified and implicitly critical. Their doubts about the economic solidity of the whole EU project dented their overall confidence in its political basis. This showed that at least in their minds they saw a clear connection between the two.⁷

In this context, it is not surprising that the 2014 second White Paper has sharper language. Its preamble is also more focused: 'The EU is China's important strategic partner in China's efforts to pursue peaceful development and multi-polarity of the world and a key party that China can work with to achieve industrialization, urbanisation, IT application and agricultural modernization as well as its 'two centennial goals',' it states. 'To grow China-EU relations is an integral part of China's efforts to build long-term, steady and healthy relations with major powers and a priority in its foreign policy.' It then goes on to structure the relationship in four key areas: partnerships for peace, for growth, for reform, and for civilisation, acknowledging that there are 'differences in history, cultural tradition, political system and stage of economic development as well as the increasing competition between China and the EU in some sectors in recent years.'⁸ On the issues of Taiwan, Tibet and Human Rights, its language is particularly forceful. Dialogue on human rights can only be undertaken on the basis of 'mutual respect and

7. See Kerry Brown, 'Decision Time or Moment of Truth for China and the EU?' China Brief, Vol 11, Issue 21, Jamestown University, November 11 2011, at http://www.jamestown.org/single/?tx_ttnews%5Btt_news%5D=38659&no_cache=1#.VuWuhn2LRH0

8. Ministry of Foreign Affairs, People's Republic of China, 'China's Policy Paper on the EU: Deepen the China-EU Comprehensive Strategic Partnership for Mutual Benefit and Win-win Cooperation', 2 April 2014, http://www.fmprc.gov.cn/mfa_eng/wjdt_665385/wjzcs/t1143406.shtml

non-interference in internal affairs.’ It asks that Taiwanese political figures ‘not be allowed to visit the EU or its member states under any pretext’. It also asks that members of what it calls the ‘Dalai group’ not to be allowed to the EU ‘under any capacity.’

Perhaps the 2014 paper was partly a response to the one significant document the EU did produce in the previous decade on the broader bilateral relationship, a communication from the Commission to the European Parliament from 2006, entitled ‘EU China, Closer Partners, Growing Responsibilities’. This had asserted a series of European aspirations towards China, one of the most striking of which was to work towards political transition and reform in the PRC, to help with the building of rule of law, and to strengthen civil society.⁹ For a leadership in Beijing increasingly uneasy about phenomenon like the Colour Revolutions in the former Soviet Union states that had occurred from 2003 onwards, and the Jasmine Revolutions in the Middle East from 2010, this was statement of ominous intent. The government under Xi Jinping from 2012 became even more categorical about those seeking to work within China and with Chinese partners in order to forge what they called ‘domestic change’ unsupported by the Party state and potentially threatening to it. The 2014 White paper on the EU and China therefore does have an element of rejection, and circumscription, of prior EU positions and actions. There were areas where deeper partnership was welcome, and areas where it was rejected. The difference was that China was clearer than ever before about where it saw these to be, and wanted a relationship on its terms, rather than on those of an outsider. In particular, it was clear that China was not going to take lectures about political reform and identity from an actor it clearly saw as weak and incoherent in this area.

3. Civilisational Partners

Despite these disagreements, the relationship between the two was, and is hugely important

for a reason which is referred to, in different ways, and for different reasons, in both the 2014 White Paper from Beijing and the 2006 Communication from Brussels: intellectual partnership and knowledge links. The EU has been China's largest technology transfer partner, and has become from the period after 2000 one of its most significant intellectual property partners. Across the 28 EU member states are some of the world's best universities, and some of its most important technology companies. The EU is also a globally important producer of intellectual property. This was perhaps why the failure to lift the arms embargo had struck at China so deeply, because it felt that the links in this realm could have become even more powerful and important.

China is clearly suffering from an innovation and technology deficit. Its foreign earnings from patents are a fraction of those of the United States. Its proprietary Intellectual Property Rights is simply not internationally attractive. The desire therefore to see greater results in this area is tangible. The government does have a 15-year innovation plan running from 2006. But as one analysis has made clear, this privileges product innovation over process and other forms. In that sense it is self-limiting, showing something of the restraints of the system in which partial innovation is being attempted—allowing the embrace of economic creativity, but still placing careful restraints in political and social areas.¹⁰

Increasingly dense intellectual links, through companies, students, and people to people interaction have made it clear to the leadership that a major relationship has been forged, and one that while specific and important, has transcended the traditional security or political sphere. When Xi as the new president of China after 2013 visited Brussels, the first time a Chinese Head of State had done so, in March 2014, he used very specific language to simultaneously acknowledge the difference between the two but recognise their common interests.

9. <http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex:52006DC0631>

10. See also Alice Rezkova, ‘Innovation in China’, in Kerry Brown (ed), ‘The EU China Relationship: European Perspectives: A Manual for Policy Makers’, Imperial College Press, London, 2014, pp. 383–380

The EU and China, he declared, related to each other as 'civilisational powers.' They did it on the basis that both are 'close to each other, as if in the same neighbourhood. Both China and Europe are in a crucial stage of development and facing unprecedented opportunities and challenges.' Echoing the white paper, he went on to say that they 'need to build four bridges for peace, growth, reform and progress of civilization, so that the China-EU comprehensive strategic partnership will take on even greater global significance.'¹¹

Civilisational partners is a nice moniker. It grants this disparate couple, one a group of 28 nation states, the other a fiscally centralised entity with centrally proclaimed unity, a veneer of commonality. The question is what precisely these civilisational attributes might be. How are they quantified and in what sense might they be meaningful? For the EU, too, it also raises the possibility that they might now be able to slip in Chinese judgements from being a complex amalgam of economic strengths and political and security weaknesses to something that at least on some level is cohesive and has something approaching political cohesiveness.

4. Market Economy Status

An opportunity to promote this more nuanced face of the EU and what sort of actor it is regarding China is through the question of market economy (ME) status being granted to China, something that involves accepting favourable tariffs and optimal market access. In terms of trade flows, as the figures given at the head of this essay show, the EU and China do well, but they could do a lot better. For the EU the issue is the 100 billion Euros plus in trade deficit. It has so far failed to really have its companies penetrate the Chinese domestic market, despite being present almost from the dawn of reform in 1978, and having many European companies active in China

over the last four decades. For instance, of the 28 member states, only Germany has a trade surplus with China.

Part of this is to do with EU economic strengths. For major economies like the United Kingdom, these are in the services sector, an area that has only in recent years truly developed in the People's Republic. The EU also currently lacks a bilateral free trade agreement. How can, in the words of Chinese Premier Li Keqiang, the EU and China together discover 'new areas of growth'? In what ways can their partnership work to deliver the different kinds of growth that both are seeking – sustainable, higher quality and more diverse?

Conferring ME status might be one area, and in 2016 its delivery might be imminent. It has been a bugbear of Chinese officials in their complaints about the EU for a number of years. It remains one of the very few things from the EU that China really wants. Under World Trade Organization, according to section 15(d) of the accession protocol, use of non-market methodology towards China can expire on 11 November 2016. The Chinese position is that the EU has to grant ME status after that date, although there is much argument about this, with EU lawyers saying this is only subject to it fulfilling certain conditions. The one issue there is more certainty about is that the final decision remains a largely political rather than economic one.¹² The paradox is that a political decision (EU conferring of ME for China) may well be the best route to a much better economic relation. The issue is that up till now, the EU has got the two the wrong way around and striven for economic wins first, before going for political ones.

5. Potential Negative and Positive Impact of Market Economy Status

Chinese officials have gone on record with claims that not getting ME status from

11. 'Speech By H.E. Xi Jinping President of the People's Republic of China At the College of Europe', 1st April 2014, file:///C:/Documents%20and%20Settings/Kerry%20Brown/My%20Documents/Downloads/speech_by_xi_jinping%20(4).pdf

12. See 'Granting Market Economy Status to China: An Analysis of WTO Law and of Selected WTO Members' Policy', European Parliament, November 2015, at [http://www.europarl.europa.eu/RegData/etudes/IDAN/2015/571325/EPRS_IDA\(2015\)571325_EN.pdf](http://www.europarl.europa.eu/RegData/etudes/IDAN/2015/571325/EPRS_IDA(2015)571325_EN.pdf)

Europe in 2016 would be to treat Chinese businesses in 'unfair, unjust, unreasonable and discriminatory' ways and would be '[an evasion of] obligations under international treaty'.¹³ It is clear that successful accession to ME status by Beijing really matters to the Chinese Government. It would be viewed by them as a major victory for the Communist Party diplomacy on the international stage and would invigorate support and prestige for their leadership.

Despite this, it is difficult not to sympathise with some of the arguments put forward in the EU that once it had ME status conferred on it, China would seek to exploit newly found economic advantages that promote the economic success of its existing exports into Europe even more ruthlessly. In this context, the deficit in trade between the EU and China might go up rather than down. China could, for instance, set a higher natural value on the exported goods of its companies into Europe, thus dulling the effect of anti-dumping duties and meaning that it could still flood the market competing with local ones which had been made with high levels of state subsidy back in the PRC. Under ME status, importing countries stand to lose the wide discretion granted to them in their independent fair value calculations for anti-dumping purposes. As a non-market economy now, China can have this treatment but not after its status changes.

The position consistently held by the European Commission which holds the competency to undertake trade negotiations on behalf of the EU¹⁴ is that Chinese Government involvement in business amounts to a level of intervention that substantively negates deserving market economy status. This includes Chinese state ownership in a majority of China's largest and most strategically important enterprises, the entrenchment of top cadres and their family members in significant managerial posts and state financing through state

ownership of state and commercial banks, for example. Moreover, if China retains its non-market economy status, there remains flexibility in the methodology by which the market value of Chinese products (in China) for import can be calculated in anti-dumping regulations. This is significant in the European position as it has politico-economic implications. The onus at the moment is on China to prove firms are operating under market conditions. The European Policy think tank in Washington have forecast that, were China to be allowed this favourable kind of access under its current economic model, then the reduction in EU outputs would potentially come to 1–2 per cent of gross domestic product, jeopardising 1.7 million to 3.5 million jobs.¹⁵ It is for this reason that work unions and other trade bodies in the EU have so far opposed ME status for China. On these grounds, therefore, conferring ME status would be risky.

6. Conclusion

Despite this, the simple fact is that ultimately the decision on granting China ME status is going to be primarily on political, not economic, grounds. While the EU and China perform well in the economic realm, the pretence that they can best relate to each other only in this area is now largely untenable. Like it or not, their relationship in the last two decades has grown increasingly political. They are diplomatic actors with each other in the Middle East, allies in the fight against climate change and have a vested interest in a stable global governance and finance system. Through granting ME status, the EU has the opportunity to strengthen strategic ties with China which, while economically risky, do bring political rewards that will eventually serve to upgrade their relationship, probably quickly.

Not that the economic side is unimportant. The EU does in 2016 need to seek more urgently new areas of economic growth. In that sense, it is in the same boat as China. A good quality deal which might contain more means for European companies to get access into

13. Statements made by Chinese foreign ministry spokesperson Lu Kang in December, 2015. Link: <http://www.chinese-embassy.org.uk/eng/HotTopics/fyrth/t1328793.htm>

14. But not that of the United Kingdom, the Netherlands or the Nordic countries, who accept China's market economy status. See <https://euobserver.com/eu-china/131801>

15. *ibid*

China would be the optimum outcome. There may be potential economic losses from granting ME status, and the EU would be making a gamble. The issue is whether there is confidence that these can be offset against more EU penetration to Chinese markets. This is an issue that the EU had to commit itself to, because the impact of the transition being undertaken in China towards a more service sector orientated model would be one that clearly suited the EU's strengths. Not doing everything to position itself competitively while others (like Australia, for instance) are signing bilateral free trade deals with the PRC means eroding its competitive position. In the end, no one truly knows what the impact of ME status for China would be in Europe. But they do know

that without greater effort and something new that reorders and reenergizes the relationship, it risks becoming increasingly moribund. As an example of where politics takes precedence over economics, this case is highly illustrative. The rewards for both are higher if they conceptualise themselves in a different way rather than just as mutual trade blocks. 'Civilisational powers' might be one way of doing that.

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